IN THE UNITED STATES BANKRUPTCY COURT FOR THE EASTERN DISTRICT OF TENNESSEE

In re

Case No. 03-36809

GOVERNOR'S CROSSING
OUTLET MALL, LLC

Debtor

MEMORANDUM ON MOTION FOR RELIEF FROM AUTOMATIC STAY AND ON MOTION TO EXCUSE CUSTODIAN

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RICHARD STAIR, JR.
UNITED STATES BANKRUPTCY JUDGE

Before the court are the Motion of Wells Fargo for Relief from the Automatic Stay (Motion for Relief) and the Motion for an Order Pursuant to 11 U.S.C. §543(d)(1) to Excuse Custodian from the Requirements of 11 U.S.C. §543(a) and 11 U.S.C. §543(b)[1] (Motion to Excuse Turnover), both filed by Wells Fargo Bank Minnesota, N.A. (Wells Fargo), as Trustee for the registered holders of Morgan Stanley Capital I, Inc., Commercial Mortgage Pass-Through Certificates, Series 1999-FNV1, on January 22, 2004. In its Motion for Relief, Wells Fargo requests relief from the automatic stay to allow it to enforce its lien on certain real property of the Debtor. In its Motion to Excuse Turnover, Wells Fargo seeks an order excusing a state court-appointed receiver from the statutory mandate to turnover property to the Debtor and provide an accounting therefor. The Debtor opposes both Motions.

The trial on these contested matters was held on April 19 and 20, 2004. The record before the court consists of the Joint Stipulation filed by the parties on March 4, 2004, twenty-four exhibits introduced into evidence, and the testimony of Theodore Merkle, III, John Cheadle, William Scott Bradford, Kenneth R. Woodford, and Phillip Don Collier.

This is a core proceeding. 28 U.S.C.A. § 157(b)(E) and (G) (West 1993).

[1] The Motion to Excuse Turnover was joined with a Motion for the Entry of an Order Finding That Rents are Not Property of the Debtor's Estate. The rent issue, discussed briefly herein at page 6, was resolved pursuant to an Order entered on March 22, 2004.

I

On December 24, 1998, the Debtor executed a Promissory Note (Note) in favor of Finova Realty Capital, Inc. in the amount of $9,700,000.00. TRIAL EX. 1. The Note was secured by a Deed of Trust and Security Agreement (Deed of Trust) dated December 24, 1998, and a UCC-1 Fixture Filing, both of which were recorded on December 31, 1998, with the Register of Deeds for Sevier County, Tennessee. TRIAL EX. 2; TRIAL EX. 3. Additionally, the parties entered into an Assignment of Leases and Rents dated December 24, 1998, that was also duly recorded. TRIAL EX. 5. Pursuant to the Deed of Trust, the Debtor pledged as collateral the real property, improvements, easements, fixtures and personal property, leases, insurance proceeds, condemnation awards, tax certiorari, licenses, intangibles, and other rights relating to the Governor's Crossing Outlet Mall (collectively, Mall Property) located in Sevier County, Tennessee. The Mall Property itself consists of approximately 18 acres of real property, owned in fee simple by the Debtor, which has been improved with 135,000 square feet of retail space.

Under the terms of the Note, the Debtor was required to make monthly payments of $71,175.16. TRIAL EX. 1. In addition to paying principal and interest, the Debtor was required to pay one-twelfth of its property taxes and insurance into an Escrow Account, from which the lender would then pay these expenses. TRIAL EX. 2. In the event of default under the terms of the Note and Deed of Trust, any sums remaining in the Escrow Account could be applied, at the lender's discretion, towards payment of taxes and insurance, payment of interest on the

unpaid principal balance of the Note, payment of the unpaid principal balance, or any other sums payable under the terms of the Note and Deed of Trust. TRIAL EX. 2.

On August 2, 1999, Finova Realty Capital, Inc. recorded a UCC-3 Assignment, assigning the Debtor's Fixture Filing to Norwest Bank Minnesota, N.A., which has since been purchased by Wells Fargo. TRIAL EX. 4. That same date, Finova Realty Capital, Inc. also recorded an Assignment of Deed of Trust and Security Agreement in favor of Norwest. TRIAL EX. 6. Morgan Stanley Capital I, Inc., Commercial Mortgage Pass-Through Certificates, Series 1999-FNV1 (Morgan Stanley), is the current holder of the Note, and Wells Fargo, as Trustee for Morgan Stanley, is authorized to proceed in this action. Wells Fargo employs CapMark Services, L.P. (CapMark) for the routine servicing of its loans, and it employs Criimi Mae Services (Criimi Mae) as its agent for the administration of its special services accounts, including loans that have matured, are delinquent, are in default, or where default appears imminent.

In January 2003, the Debtor notified its contact with CapMark that it was experiencing financial strains, causing it to fall behind on payment on the Note, and proposing to use a portion of its Reserve Account to bring the payments current. TRIAL EX. 15. After receiving no written response, in February 2003, the Debtor again corresponded with CapMark, twice requesting assistance in halting any further delay in payments by use of funds in the Reserve Account. TRIAL EX. 16; TRIAL EX. 17. The Debtor defaulted under the terms of the Note, and on March 4, 2003, was notified that its loan was being transferred to Criimi Mae for servicing. TRIAL EX. 18. On April 7, 2003, the Debtor sent a proposal to Criimi Mae, suggesting a

workout that would "put the Mall back on schedule with payments current as of August 1, 2003." TRIAL EX. 19. The Debtor never received any written responses to its proposed cure of the default.

On November 10, 2003, Wells Fargo gave the Debtor written notice that it was accelerating the balance due under the Note and demanding payment in the aggregate amount of $10,005,927.14 no later than November 13, 2003. TRIAL EX. 24. The Debtor did not pay the accelerated balance, and on November 24, 2003, Wells Fargo filed a Sworn Complaint for Receiver in the Chancery Court for Sevier County, Tennessee. Pursuant to Wells Fargo's Complaint, the Chancery Court entered an Ex Parte Order of Appointment of Receiver on November 24, 2003, whereby John Cheadle was appointed receiver. TRIAL EX. 7. Pursuant to this Order, Mr. Cheadle was directed to take immediate possession of the Mall Property and was authorized to "collect all rent payments, funds and accounts receivable" and to pay all operating costs of the Debtor. TRIAL EX. 7.

The Debtor filed the Voluntary Petition commencing its Chapter 11 bankruptcy case on December 16, 2003. TRIAL EX. 34. Also on December 16, 2003, the Debtor served a letter upon Mr. Cheadle, the receiver, demanding that he surrender the Debtor's assets pursuant to 11 U.S.C.A. § 543(a) (West 1993) and for an accounting pursuant to 11 U.S.C.A. § 543(b) (West 1993). TRIAL EX. 13.

Wells Fargo filed the Motion for Relief and the Motion to Excuse Turnover, along with a Motion for the Entry of an Order Finding that Rents are Not Property of the Debtor's Estate.[2] In a Memorandum filed March 22, 2004, and the corresponding Order entered on the same date, the court held that the rents associated with the operation of the Mall Property are not property of the bankruptcy estate but are the property of Wells Fargo because the Assignment of Rents recorded on December 31, 1998, was an absolute assignment of all rights and interests therein from the Debtor to Finova Realty Capital, Inc., predecessor in interest to Morgan Stanley.

II

The first issue to be addressed is whether Wells Fargo is entitled to relief from the automatic stay and/or adequate protection. Requests for relief from the automatic stay are governed by 11 U.S.C.A. § 362(d), which provides, in material part:

> (d) On request of a party in interest and after notice and a hearing, the court shall grant relief from the stay provided under subsection (a) of this section, such as by terminating, annulling, modifying, or conditioning such stay—
>
> > (1) for cause, including the lack of adequate protection of an interest in property of such party in interest;
> >
> > (2) with respect to a stay of an act against property under subsection (a) of this section, if—
> >
> > > (A) the debtor does not have an equity in such property; and
> > >
> > > (B) such property is not necessary to an effective reorganization[.]

[2] *See supra* note 1.

11 U.S.C.A. § 362(d) (West 1993 & Supp. 2004). The automatic stay provides a debtor with "an opportunity to protect [its] assets for a period of time so that [its] resources might be marshaled to satisfy outstanding obligations." *Laguna Assocs. Ltd. P'ship v. Aetna Cas. & Sur. Co. (In re Laguna Assocs. Ltd. P'ship)*, 30 F.3d 734, 737 (6th Cir. 1994) (citing, among others *In re Winshall Settlor's Trust*, 758 F.2d 1136, 1137 (6th Cir. 1985) ("The purpose of a Chapter 11 reorganization is to assist financially distressed business enterprises by providing them with breathing space in which to return to a viable state.")).

A

Wells Fargo first requests relief under § 362(d)(1), stating that cause exists because the court has determined that rents are not the Debtor's property. Additionally, Wells Fargo argues that the Debtor has not offered it any sort of adequate protection, which also justifies relief. The Debtor argues that adequate protection is not an issue because the Debtor is not using any of Wells Fargo's collateral. Also, the Debtor argues that cause does not exist because the Mall Property is not depreciating, nor is there any evidence of bad faith or mismanagement by the Debtor.

A creditor seeking relief from the automatic stay under § 362(d)(1) "bears the burden of producing evidence establishing a legally sufficient basis for such relief[.]" *In re Planned Sys., Inc.*, 78 B.R. 852, 860 (Bankr. E.D. Ohio 1987). In order to obtain relief from the stay for lack of adequate protection, the creditor must establish a *prime facie* case, including proof that the debtor owes a debt to the creditor, that the creditor possesses a valid security interest

securing the debt, and that the collateral securing the debt is declining in value while the debtor has failed to provide the creditor with adequate protection of its interest in the collateral. *In re Cambridge Woodbridge Apts., L.L.C.*, 292 B.R. 832, 841 (Bankr. N.D. Ohio 2003); *Planned Systems*, 78 B.R. at 860.

The Bankruptcy Code addresses adequate protection as follows:

> When adequate protection is required under section 362 . . . of this title of an interest of an entity in property, such adequate protection may be provided by—
>
> > (1) requiring the trustee to make a cash payment or periodic cash payments to such entity, to the extent that the stay under section 362 of this title . . . results in a decrease in the value of such entity's interest in such property;
> >
> > (2) providing to such entity an additional or replacement lien to the extent that such stay . . . results in a decrease in the value of such entity's interest in such property; or
> >
> > (3) granting such other relief, other than entitling such entity to compensation allowable under section 503(b)(1) of this title as an administrative expense, as will result in the realization by such entity of the indubitable equivalent of such entity's interest in such property.

11 U.S.C.A. § 361 (West 1993).

Adequate protection safeguards a secured creditor's interest in its depreciating collateral during the pendency of the automatic stay. *See United Sav. Ass'n of Tex. v. Timbers of Inwood Forest Assocs., Ltd.*, 108 S. Ct. 626, 630 (1988). Courts must consider "the nature of the creditor's interest in the property, the potential harm to the creditor as a result of the property's decline in value and the method of protection" when making a determination of adequate protection. *In re Plabell Rubber Prods.*, 137 B.R. 897, 900 (Bankr. N.D. Ohio 1992)

(quoting *Matter of Braniff Airways, Inc.*, 783 F.2d 1283, 1286 (5th Cir. 1986)). However, "[t]he concept of adequate protection was not designed or intended to place an undersecured or minimally secured creditor in a better post-filing petition [sic] than it was in before the stay." *Planned Systems,* 78 B.R. at 862 (quoting *In re Smithfield Estates, Inc.*, 48 B.R. 910, 914-15 (Bankr. D.R.I. 1985)). Because "[a]dequate protection is never necessary unless there is a threat to the value of the encumbrance[, in order t]o determine whether a secured creditor's interest is adequately protected[, courts should consider] (1) the value of the interest; (2) the risk that the value of the encumbrance will decline; and (3) whether the debtor's adequate protection proposal protects value against such risks." *Cambridge Woodbridge Apts.*, 292 B.R. at 841.

In this case, Wells Fargo's interest in the Mall Property is adequately protected by the rents, which the court has determined are the property of Wells Fargo, to be applied towards its debt. Additionally, for reasons hereinafter set forth in its discussion under § 362(d)(2), the court finds that the Mall Property is not declining in value, nor is Wells Fargo, at this time, subject to any risk of its interest declining.

B

Even though it is not entitled to relief from the automatic stay under § 362(d)(1), Wells Fargo may be entitled to relief under § 362(d)(2) if there is no equity in its collateral, and the Mall Property is not necessary for the Debtor's effective reorganization. *See* 11 U.S.C.A. § 362(d)(2). Wells Fargo bears the burden of establishing that there is no equity,

and if it meets this burden, the Debtor must prove the necessity of the collateral for an effective reorganization. *See* 11 U.S.C.A. § 362(g). However, if Wells Fargo cannot establish the lack of equity, the inquiry ends, and it is not entitled to relief from the stay under § 362(d)(2). *See* 11 U.S.C.A. § 362(d)(2); *Sumitomo Trust & Banking Co. v. Holly's Inc. (In re Holly's Inc.)*, 140 B.R. 643, 697 (Bankr. W.D. Mich. 1992) ("Because § 362(d)(2) is drafted in the conjunctive, both prongs must be satisfied to grant relief from the stay.").

1

For the purposes of § 362(d)(2), equity is defined as "the value, above all secured claims against the property, that can be realized from the sale of the property for the benefit of the unsecured creditors." *Holly's, Inc.*, 140 B.R. at 697 (quoting *Stephens Indus., Inc. v. McClung*, 789 F.2d 386, 392 (6th Cir. 1986)). As of December 16, 2003, the indebtedness owed by the Debtor to Wells Fargo was $10,293,429.60. At trial, Mr. Merkle, special servicer with Criimi Mae, provided the following breakdown of the debt: principal in the amount of $9,327,814.97, accrued interest of $283,980.14, default interest of $447,407.58, escrow for taxes of $69,557.16, escrow for insurance of $19,610.16, unpaid reserve of $92,719.08, late fees of $51,799.44, and miscellaneous expenses of $541.07. Additionally, if the Mall Property is sold or if the indebtedness is paid prior to the maturity date of January 1, 2009, the Debtor will be required to pay a defeasance penalty of approximately $2,157,725.17. Criimi Mae is currently holding $152,554.20 in reserves for tenant build-outs and improvements to the Mall Property. To date, Wells Fargo has not filed a Proof of Claim in the Debtor's bankruptcy case; however, the Debtor did not dispute these figures.

Wells Fargo avers that the Mall Property is worth $7,100,000.00, based upon the October 22, 2003 appraisal conducted by William Scott Bradford. *See* TRIAL EX. 26. Mr. Bradford is employed as a Senior Real Estate Analyst with CB Richard Ellis, Inc. in Atlanta, Georgia. He is an associate member of the Appraisal Institute, is certified in six states, and has approximately fifteen years experience as an appraiser. Over the last nine years, Mr. Bradford has appraised four different outlet mall properties in Pigeon Forge and approximately fifty total across the United States.

Mr. Bradford testified that he used the Income approach, which requires the determination of a capitalization rate. Because there is no direct formula for determining a direct capitalization rate, Mr. Bradford stated that he relies upon various factors and his years of experience to assign the capitalization rate. He also researches sales comparables for their capitalization rates, reviews internal reports published by CB Richard Ellis, Inc., and discusses the rates with an analyst in his company's Chicago office. Following that basic procedure, Mr. Bradford based his appraisal, valuing the Mall Property at $7,100,000.00, on a review of the Mall Property itself, along with the Debtor's financial documents provided to him by the Debtor and Wells Fargo. Factors he considered relevant in his analysis included the age of the Mall property, its tenancy rates, lease terms, and the tenant profile. While Mr. Bradford testified that outlet malls, in general, carry a greater degree of risk than other retail establishments because of their specialized nature, he specifically noted that the Debtor had visibility issues because it did not directly face the main parkway in Pigeon Forge, and it was difficult to see the Mall Property from the parkway. Nevertheless, his report rates the Mall

Property's condition as "good." TRIAL EX. 26. Based upon the aforementioned factors, Mr. Bradford assigned the Mall Property a 14% capitalization rate.

As for the numbers affecting his decision, Mr. Bradford noted that the Debtor's income had decreased from $1,243,927.00 in 2002 to $952,841.00 for 2003, annualized from January to September. He also testified that the Debtor's expenses, per its November 2003 balance sheet, do not conform to industry norms because they do not list items such as management fees or reserve allowances that are typically included by similar entities. *See* TRIAL EX. 35. Another area of concern for Mr. Bradford was the failure of the Debtor to obtain expense reimbursements from its tenants, which he stated was a general provision in most retail leases. Additionally, Mr. Bradford stated that he did not consider debt structure in his analysis; rather, he assumes that the property being appraised is not leveraged. Finally, Mr. Bradford's appraisal did not include a separate land valuation.

Mr. Bradford testified that he obtained the statistical information regarding Sevier County's business and population data from the Sevier County Chamber of Commerce. Mr. Bradford testified that he only included information that he considered relevant in the Area Analysis section of his appraisal, including information regarding the populations of Sevier County for a one-, three-, and five-mile radius from the Mall Property, based upon the 2000 Census and the growth trends and employment figures, including gross sales attributable to Pigeon Forge's outlet mall sales from 1989 through 2002. TRIAL EX. 26.

In contrast, the Debtor argues that the value of the Mall Property is $10,000,000.00, as reflected by the March 19, 2004 appraisal conducted by Kenneth R. Woodford. TRIAL EX. 49. Mr. Woodford is a member of the Appraisal Institute, holding MAI and SRA certifications, and is licensed by the State of Tennessee as a Certified General Appraiser. He has approximately thirty years experience, generally concerning commercial and industrial properties, and his practice primarily centers around Knoxville and surrounding counties in East Tennessee, including Sevier County.

Mr. Woodford has appraised the Mall Property on two occasions. His first appraisal occurred in August 1998, just after the Mall was completed, at which time he recalled valuing the Mall Property at $9,000,000.00 "as is" and assigning a stabilized value, after it was leased out, of $14,500,000.00. Mr. Woodford's second appraisal occurred on March 19, 2004, and he testified that he arrived at the final value of $10,000,000.00 after combining the results from the Sales Comparable approach, the Income approach, and the Cost approach.[3] Additionally, Mr. Woodford has appraised the land, without improvements, at $3,300,000.00, based upon a comparison of ten recent land sales in the area.

To arrive at his valuation, Mr. Woodford relied upon similar demographics and regional data as relied upon by Mr. Bradford, plus additional regional information regarding anticipated developments in their planning and implementation stages. He also relied upon

[3] Mr. Woodford testified that under the Sales Comparable approach, he valued the Mall Property at $10,975,000.00. Using the Income approach, and a capitalization rate of 9.25%, the Mall Property had a value of $9,675,000.00. Finally, under the Cost approach, he deduced that the value of the Mall Property was $11,400,000.00.

the income and expense information received from the Debtor, in addition to his personal assessment of the Mall Property. Like Mr. Bradford, Mr. Woodford testified that it was typical for tenants in other outlet mall centers to pay reimbursement of expenses, and that of the Debtor's tenants, only five or six did so. Mr. Woodford also attributed the Debtor's decline in income to loss of tenants, as well as the renegotiation of leases at lower rates. Mr. Woodford also noted that the Debtor's expenses did not include management fees and/or tenant reserves; however, he testified that it was his understanding that the Debtor provided in-house management and maintenance, and thus, those expenses were included in the Debtor's overall payroll figures.

Based upon the evidence presented, the court finds that the $10,000,000.00 value more accurately reflects the value of the Mall Property. First, Mr. Woodford's appraisal is more recent than Mr. Bradford's appraisal, and he has relied upon more recent statistical data concerning the area and its business development, primarily concerning developments recently completed, those presently being developed, and those in their final planning stages. Additionally, Mr. Woodford has inspected and appraised the Mall Property on two separate occasions, when it was first developed in 1998, and most recently, in March 2004. And, as he testified, Mr. Woodford primarily focuses his appraisal practice in East Tennessee, having appraised hundreds of properties in this area over his thirty years of experience, and thus, he is personally more familiar with Sevier County than is Mr. Bradford, who lives in Atlanta and has appraised a total of four properties in the Pigeon Forge area.

The court is also more persuaded by Mr. Woodford's cumulative valuation, whereby he assessed the Mall Property using not only the Income approach employed by Mr. Bradford, but also assessing valuation under the Sales Comparable and Cost approaches.[4] The court believes that this is a more accurate valuation in light of the differing approaches to accommodate variances in the data relied upon. Additionally, Mr. Woodford's appraisal includes information and data concerning upcoming developments that has the potential to greatly impact the Debtor's business, including road extensions directly in front of the Mall Property. Specifically, Phillip Don Collier, an owner and manager of the Debtor, testified that Sevier County is currently in the process of constructing a shortcut to the Dollywood theme park from the main parkway that would cut directly in front of the Mall Property. Once completed in the fall of 2005, it is anticipated that traffic past the Mall Property will increase by approximately 33,000 vehicles per day, which would almost certainly result in a substantial increase in business and revenues. At that point, the Debtor would be in a better position to renegotiate its leases to obtain higher rents, to attract higher quality tenants, and to market and carve-out portions of its parking lot to restaurants.[5] This information may not have been known by Mr. Bradford, and it was not considered by Mr. Bradford in his appraisal report, although he testified that he did consider future factors that might impact the value

[4] Mr. Bradford's appraisal report does contain a Sales Comparable Analysis, finding a valuation of $7,000,000.00; however, he testified that in making his assessment, he uses the comparable sales primarily to compare capitalization rates. He also stated that in this case, he only relied upon the Income approach analysis, which is the approach he most often employs.

[5] As historical support for his estimations regarding business increases, Mr. Collier testified that in 1998, a gas line rupture in Pigeon Forge forced the closure of the main parkway through Pigeon Forge, and traffic was re-routed in front of the Mall Property. On that one day, the Mall Property tenants enjoyed a 100% increase in business.

of the Mall Property. The court agrees that this road extension could have a substantial impact upon the Debtor's business and income once completed.

The court is also concerned with some of the assumptions made by Mr. Bradford and included in his appraisal analysis. First, Mr. Bradford testified that he generally assigns a capitalization rate between 10% and 14% for outlet malls, based upon a greater degree of risk involved. Additionally, he testified that because outlet malls do not fit within the same general parameters as do other retail spaces, including strip malls, he was forced to extrapolate in his determination of a capitalization rate. While the court does not quarrel with Mr. Bradford's experience and information, there is danger in assuming that all outlet malls present a high degree of risk based upon the specialization of their tenants, especially without any evidence to substantiate this assertion. Moreover, in this case, Mr. Collier testified that even though it houses what may be referred to as "outlet" tenants, for all intents and purposes, the Mall Property is most closely related to a strip mall, in that it contains no interior corridors or walkways, and it is one-story. The photographs contained in both appraisal reports support Mr. Collier's description of the layout of the Mall Property. TRIAL EX. 26; TRIAL EX. 49.

Additionally, the court is concerned with several liberties taken by Mr. Bradford regarding listed operating expenditures of the Debtor. First, Mr. Bradford testified that it was his experience that malls typically attributed anywhere from 3% to 5% of gross revenues to payment of a management fee. However, he noted that the Debtor did not include any management fees within its operating expenses, which he believed inflated the Debtor's actual

income. Therefore, Mr. Bradford testified that he assumed a 5% management fee in his appraisal analysis, which he included to increase the Debtor's listed operating expenses and to decrease the Debtor's income.

Mr. Bradford also testified that the Debtor's expenses did not include a reserve for replacement, tenant build-outs, and other major repairs. The appraisal reflects that replacement reserves typically range from $.10 to $.20 per square foot, and even though the Debtor did not include any reserves in its expenditures, Mr. Bradford included a projected reserve expense of $.15 per square foot in his analysis. TRIAL EX. 26.

Similarly, Mr. Bradford testified that he believed that the Debtor's estimate for marketing expenses of $.25 per square foot was inadequate based upon what other outlet centers spent, arguing that the less that a center markets, the lower traffic it enjoys, resulting in lower sales. To remedy this presumed deficiency, for his appraisal, Mr. Bradford adjusted the Debtor's marketing expenses to $.75 per square foot, a number he felt was more in line with the industry standard.

Wells Fargo questioned the Debtor's failure to include management fees and/or a replacement reserve in its operating expenses. When asked about the lack of these fees and expenses, Mr. Collier testified that Collier Development, Inc., a corporation in which he is a shareholder with other members of his family, has been providing management services to the Debtor for no charge, and that it would continue doing so as long as necessary to reorganize. Likewise, Mr. Collier testified that Paula Smeltser, the on-site manager, has been

compensated by Hotel Partners, another family-owned and operated entity, which is also willing to continue supplementing the Debtor. Additionally, Mr. Collier testified that the Debtor has a two or three person in-house maintenance crew that makes all necessary repairs, that the Mall Property is in excellent condition, and that he anticipates no major repairs will be needed in the short-term. Therefore, the Debtor has not allocated anything beyond costs of repairs within those parameters.

With regards to the marketing expenses listed, Mr. Collier testified that, in the past, the Debtor has spent more on marketing, including paying radio stations to do live remotes from the Mall Property in order to attract additional customers. Mr. Collier stated that because these ventures seemed to attract a majority of local patrons seeking the free prizes and merchandise offered by the radio stations, these practices were not cost-effective, and they were discontinued. Mr. Collier also testified that the Debtor has spent approximately $35,000.00 on a giant 35-foot electronic sign that sits on the main parkway near the WalMart Supercenter. Additionally, Mr. Collier testified that the Mall Property is surrounded by several restaurants, including TGI Fridays, Mr. Gatti's, Fuddruckers, Texas Roadhouse, and Up the Creek. Other tourist attractions and businesses in the immediate vicinity of the Mall Property are Gem Mining, Nascar Café, Governor's Inn Hotel, Fairfield Resorts timeshares, Rainforest Adventures Park, and a branch of Branch Banking & Trust.

In contrast to Mr. Bradford's appraisal report, Mr. Woodford took this information into account when he performed his Income approach analysis. With regards to the lack of management fees and a replacement reserve, Mr. Woodford included them within the payroll

expenses of the Debtor and did not assume additional costs not reflected within the Debtor's own listed expenditures. While the court recognizes that there are market averages and standards for expenditures routinely incurred by other mall properties within Mr. Bradford's experience, the Debtor has offered credible reasons why such expenses are not included in its regular expenditures, primarily because these costs have been attributed to other categories that are included within listed expenditures. In this case, Mr. Bradford's assumptions and additions based upon industry "norms" unfairly inflated the Debtor's expenditures, resulting in decreased income and a decreased final valuation.

Based upon a $10,000,000.00 valuation, there is still no equity in the Mall Property. As of the date of the bankruptcy filing, December 16, 2003, the Debtor's indebtedness owed to Wells Fargo was $10,293,429.60. Wells Fargo is currently holding $152,554.20 in reserves; however, even if Wells Fargo were to credit those funds toward the debt owed by the Debtor, the outstanding balance would still be greater than the $10,000,000.00 valuation by $140,875.40. Because there is no equity in the Mall Property, the burden shifts to the Debtor to prove that it cannot successfully reorganize without the Mall Property.

2

To satisfy § 362(d)(2)(B), the Debtor must establish that it is attempting to effectuate a successful reorganization, within a reasonable time, and that the Mall Property is necessary therefor. *See Timbers of Inwood Forest Associates*, 108 S. Ct. at 633. Moreover, the Debtor must provide more than just an assertion that reorganization is not possible without the

collateral. *In re St. Peter's Sch.*, 16 B.R. 404, 408 (Bankr. S.D.N.Y. 1982). At a minimum, the Debtor must make a showing that:

> (1) It is moving meaningfully to propose a plan of reorganization. The older or simpler a case or "iffier" the business is, the stronger that showing must be.
>
> (2) The proposed or contemplated plan has a realistic chance of being confirmed . . . [and] must provide that:
>
> > (a) The lender's allowed secured claim can be realistically valued and paid over time . . . from the debtor's net operating income generated by the property, or
> >
> > (b) Some other means of proposing a confirmable plan are realistically contemplated. These may include new capital contributions, sale to a third party or other options sanctioned by the Bankruptcy Code.
>
> (3) The proposed or contemplated plan is not patently unconfirmable.

In re Ashgrove Apts. of Delakb County, Ltd., 121 B.R. 752, 756-57 (Bankr. S.D. Ohio 1990); *see also Creekstone Apts. Assocs., L.P. v. Resolution Trust Corp. (In re Creekstone Apts. Assocs., L.P.)*, 168 B.R. 639, 642 (Bankr. M.D. Tenn. 1994); *In re Snapwoods Apts. of Dekalb County, Ltd.*, 153 B.R. 524, 526 (Bankr. S.D. Ohio 1993). A plan may be "somewhat obscure or vague as long as it is plausible that a successful reorganization may occur." *Holly's Inc.*, 140 B.R. at 701.

There appears to be no real dispute that if the Debtor is to successfully reorganize, rather than simply liquidate, it must retain possession of the Mall Property. The Debtor has two assets, Phase I which is the Mall Property and Phase II, an unimproved tract consisting of approximately four acres. A proposal to sell Phase II has already been filed with the court and will be heard on May 11, 2004. In the event that Phase II is sold, the Debtor seeks to

realize approximately $220,000.00 after setting aside funds sufficient to pay all unsecured creditors. At that point, the Debtor's sole remaining asset will be the Mall Property.

Wells Fargo questions whether the Debtor can successfully reorganize. First, it focuses on the Debtor's decline in income. Second, Wells Fargo argues that because the Debtor does not have any other sources of income other than the rents, which are property of Wells Fargo, it cannot successfully reorganize because it cannot pay the regular operating expenses, taxes, and insurance associated with the operation of the Mall Property.

Both appraisal reports reflect a decrease in the Debtor's income over the past few years. When questioned about the decline in income, Mr. Collier testified that the large majority of the decline resulted from the loss of five tenants in 2002, three of which filed for bankruptcy. In an attempt to avoid additional cash flow problems, the Debtor negotiated some short-term leases and renegotiated other lease terms in order to fill empty space. Also, there is no question that the Pigeon Forge area and most of the tourism industry has suffered losses, particularly since the tragedies of September 11, 2001. However, Mr. Collier testified that he believes that the area is enjoying an upswing in tourists again, which will obviously result in increased volume in customers and increased revenues. Mr. Woodford's appraisal report also reflects increases in Pigeon Forge's gross business receipts, along with an increase in visitation from tourists enjoyed by Sevier County. See TRIAL EX. 49.

Also significant to the equation is the fact that the Debtor only filed its bankruptcy petition in December 2003. It has been in bankruptcy for just over four months, and the court

believes that it is entitled to time to effectuate a successful plan of reorganization. Whether it can do so given its inability to utilize the tenant rents generated from the operation of the Mall Property in formulating its plan remains to be seen. For this reason, the court is not inclined to allow the Debtor an inordinate amount of time to formulate a plan of reorganization, especially if it becomes apparent that reorganization of the Mall Property is not possible or feasible. Therefore, the court will revisit Wells Fargo's Motion for Relief in October, in the event a plan has not been confirmed. In the meantime, there will be nothing to prohibit Wells Fargo from bringing future issues of adequate protection before the court, such as the failure to pay the insurance when due in July 2004 or the failure to cure the property tax arrearage.[6]

III

The next issue before the court is whether Mr. Cheadle, the receiver appointed by the Sevier County Chancery Court, may be excused from turning over the Debtor's property to the Debtor. Upon the filing of a bankruptcy petition, a previously-appointed receiver must "cease administration, deliver property to the trustee, and account for all property [as his powers have been] . . . superseded, terminated, deactivated, [and he has become] devoid of power" by the bankruptcy. *In re Rimsat, Ltd.*, 193 B.R. 499, 502 (Bankr. N.D. Ind. 1996) (citations omitted). Pursuant thereto, 11 U.S.C.A. § 543 provides:

[6] Mr. Collier testified that a portion of the $220,000.00 anticipated by the Debtor from the sale of Phase II will be used to pay the property tax arrearages and insurance premiums. The court expects the Debtor to promptly pay these obligations and to properly maintain the Mall Property. Should the Mall Property begin to fall into disrepair, adequate protection issues will again be of concern.

(a) A custodian with knowledge of the commencement of a case under this title concerning the debtor may not make any disbursement from, or take any action in the administration of, property of the debtor, proceeds, product, offspring, rents, or profits of such property, or property of the estate, in the possession, custody, or control of such custodian, except such action as is necessary to preserve such property.

(b) A custodian shall—

> (1) deliver to the trustee any property of the debtor held by or transferred to such custodian, or proceeds, product, offspring, rents, or profits of such property, that is in such custodian's possession, custody, or control on the date that such custodian acquires knowledge of the commencement of the case; and
>
> (2) file an accounting of any property of the debtor, or proceeds, product, offspring, rents, or profits of such property, that, at any time, came into the possession, custody, or control of such custodian.

(c) The court, after notice and a hearing, shall—

> (1) protect all entities to which a custodian has become obligated with respect to such property or proceeds, product, offspring, rents, or profits of such property; [and]
>
> (2) provide for the payment of reasonable compensation for services rendered and costs and expenses incurred by such custodian[.]

. . . .

(d) After notice and hearing, the bankruptcy court—

> (1) may excuse compliance with subsection (a) [or] (b) . . . of this section if the interests of creditors and, if the debtor is not insolvent, of equity security holders would be better served by permitting a custodian to continue in possession, custody, or control of such property, and
>
> (2) shall excuse compliance with subsections (a) and (b)(1) of this section if the custodian is an assignee for the benefit of the debtor's creditors that was appointed or took possession more than 120 days before the date of the filing of the petition, unless compliance with such subsections is necessary to prevent fraud or injustice.

11 U.S.C.A. § 543. "Subsection 543(b) absolutely requires a custodian to deliver to the bankruptcy trustee, or debtor-in-possession, where no trustee has been appointed, any property of the debtor that is in the possession, custody or control of the non-bankruptcy custodian." *Powers Aero Marine Servs., Inc. v. Merrill Stevens Dry Dock Co. (In re Powers Aero Marine Servs., Inc.)*, 42 B.R. 540, 543 (Bankr. S.D. Tex. 1984).

> The turnover provisions of 11 U.S.C. § 543 are part of the statutory expression of the Congressional preference that a Chapter 11 debtor be permitted to operate and control its business during the reorganization process. Moreover, that operation is for the benefit of all constituencies and is not solely for the benefit of the lender holding the primary mortgage against the debtor's property. "Generally the basic equities would favor a debtor or debtor in possession. If nothing more, a substantial weight is added to the debtor's burden of attempting to reorganize and promulgate an acceptable plan of reorganization if the debtor cannot have access to all of its assets during its initial breathing spell." The statute contemplates that property being managed by a receiver will be returned to the representative of the estate upon the commencement of a bankruptcy case by the owner.

In re Northgate Terrace Apts., Ltd., 117 B.R. 328, 332-33 (Bankr. S.D. Ohio 1990) (quoting *In re KCC-Fund V, Ltd.*, 96 B.R. 237, 239-240 (Bankr. W.D. Mo. 1989)).

Nevertheless, the bankruptcy court, in its discretion, may excuse a receiver, such as Mr. Cheadle, from compliance with § 543(a) or (b).

> A Court considering whether to exercise its discretion under section 543(d)(1) may consider several factors indicative of whether the interests of creditors would be better served. These factors have evolved to include: (1) whether there will be sufficient income to fund a successful reorganization; (2) whether the debtor will use the turnover property for the benefit of the creditors; (3) whether there has been mismanagement by the debtor; (4) whether or not there are avoidance issues raised with respect to property retained by a receiver, because a receiver does not possess avoiding powers for the benefit of the estate; and (5) the fact that the bankruptcy automatic stay has deactivated the state court receivership action.

Dill v. Dime Sav. Bank FSB (In re Dill), 163 B.R. 221, 225 (E.D.N.Y. 1994); *see also In re Lizeric Realty Corp.*, 188 B.R. 499, 506-07 (Bankr. S.D.N.Y. 1995); *In re Constable Plaza Assocs., L.P.*, 125 B.R. 98, 103 (Bankr. S.D.N.Y. 1991). The interests of the Debtor are not considered in the § 543 analysis. *Dill*, 163 B.R. at 225; *Foundry of Barrington P'ship v. Barrett (In re Foundry of Barrington P'ship)*, 129 B.R. 550, 558 (Bankr. N.D. Ill. 1991). The party seeking to excuse compliance bears the burden of proof by a preponderance of the evidence. *Lizeric Realty Corp.*, 188 B.R. at 506.

The court finds that cause does not exist to excuse compliance with § 543(a) or (b). There is no evidence of mismanagement by the Debtor, nor has the Debtor engaged in any action detrimental to its creditors whereby a receiver should be retained. Instead, the evidence presented at trial leads the court to the conclusion that the Debtor and Wells Fargo are perfectly capable of working together to achieve the goals that appointment of the receiver was intended to accomplish.

The only property in Mr. Cheadle's possession are the rents collected from the Mall tenants each month. The court has already ruled those rents are not property of the Debtor's bankruptcy estate, but instead, belong solely to Wells Fargo. Mr. Cheadle testified that, as receiver, he is working with the Debtor to collect rents from the Mall tenants, and that he has been authorized by Criimi Mae and the court to pay the monthly operating expenses from those rents. Since his appointment as receiver in November 2003, he has collected just under $400,000.00, all of which is being held in his trust account, less the approximately

$57,000.00 in paid monthly operating expenses. Mr. Cheadle testified that if the operating expenses were not paid, the Mall Property would lose value because tenants would not be properly serviced, and the real property itself would not be maintained. The Debtor disputes this conclusion.

On the other hand, Mr. Cheadle testified that the Debtor has, throughout the pendency of the receivership, cooperated with him, assisted with the collection of rents, and provided on-site management of the Mall Property through Ms. Smeltser, at no additional cost to the receivership. Additionally, there is no proof that the Debtor has ever attempted to divert the rents or has been anything other than cooperative in its dealings with Mr. Cheadle.

As for the question of whether there will be sufficient monies to fund a reorganization, Mr. Cheadle testified that he did not have knowledge whether the Debtor could pay the monthly operating expenses without use of the rents, nor had he asked if that was possible. When questioned about the ability of the Debtor to make expense payments, Mr. Collier acknowledged that the rents generated by the leases with its tenants are the only real source of income for the Mall. Nevertheless, he testified that if approved by the court, the sale of Phase II would yield funds sufficient to fully satisfy the claims of all unsecured creditors and leave the Debtor with approximately $220,000.00 in cash to be used for operating expenses of the Mall Property. Additionally, Mr. Collier testified that he and the Debtor's other owners would be available to provide other sources of income to the Debtor for payment of the Mall's expenses.

The court finds that the Debtor is capable of working with Wells Fargo to collect and turnover the rents to Wells Fargo without the necessity of the state court-appointed receiver. Accordingly, Mr. Cheadle shall be required to turnover all funds in his possession to Wells Fargo within ten days. Wells Fargo shall apply these funds in a manner appropriate under the terms of the Note and Deed of Trust. Additionally, Mr. Cheadle shall be required to file the accounting required by 11 U.S.C.A. § 543(b)(2) within fourteen days. To the extent Mr. Cheadle seeks compensation and expenses for his services as receiver, he shall file an appropriate application with this court within thirty days.[7] *See* 11 U.S.C.A. § 543(c)(2). The Debtor shall be required to provide Wells Fargo with monthly statements due for each month by the 10th day of the following month, indicating payments for general maintenance, upkeep, and related expenses associated with the Mall Property.

Finally, the court urges Wells Fargo to meet with the Debtor and Mr. Cheadle expeditiously in order to ensure a smooth transition that is satisfactory to Wells Fargo and the Debtor for payment of future rents generated from the Mall Property. The court will direct that the Debtor continue collecting the rents from its tenants to promote the stability of the Debtor and to assure tenants that they will continue to be serviced by a local manager; i.e., Ms. Smeltser, because if the tenant base erodes, so too will the collection of Wells Fargo's rents. In light of the fact that the court is requiring the Debtor to provide monthly maintenance statements to Wells Fargo, it would not be difficult to also set up a procedure

[7] Notwithstanding that the rents in Mr. Cheadle's possession are not property of the bankruptcy estate, the court deems it appropriate for the bankruptcy court to fix Mr. Cheadle's compensation because the rents will be applied to the unpaid balance of the Debtor's obligation to Wells Fargo, which will affect the amount of Wells Fargo's claim against the Debtor.

by which the rents could easily be transferred to Wells Fargo. The court will leave it to the parties to set up an appropriate device for safeguarding and transferring future rents to Wells Fargo. Wells Fargo will be required to provide the Debtor with a monthly accounting showing its application of the rents received from the Debtor.

An order consistent with this Memorandum will be entered.

FILED: April 29, 2004

BY THE COURT

/s/ Richard Stair, Jr.

RICHARD STAIR, JR.
UNITED STATES BANKRUPTCY JUDGE

IN THE UNITED STATES BANKRUPTCY COURT FOR THE EASTERN DISTRICT OF TENNESSEE

In re

Case No. 03-36809

GOVERNOR'S CROSSING
OUTLET MALL, LLC

Debtor

O R D E R

For the reasons set forth in the Memorandum on Motion for Relief From Automatic Stay and on Motion to Excuse Custodian filed this date, the court directs the following:

1. The Motion of Wells Fargo for Relief From Automatic Stay filed by Wells Fargo Bank Minnesota, N.A., as Trustee for the registered holders of Morgan Stanley Capital I, Inc., Commercial Mortgage Pass-Through Certificates, Series 1999-FNV1, on January 22, 2004, is neither granted nor denied, and the automatic stay will remain in effect pending further order of the court. Unless future adequate protection issues are sooner brought to the court's attention, the Motion of Wells Fargo for Relief From Automatic Stay will be revisited at a hearing to be held on October 15, 2004, at 9:00 a.m., in Bankruptcy Courtroom 1-C, First Floor, Howard H. Baker, Jr. United States Courthouse, Knoxville, Tennessee. At this hearing, the court will consider additional evidence and will determine whether the automatic stay should then be modified to allow Wells Fargo Bank Minnesota, N.A. to foreclose its interest in the Governor's Crossing Outlet Mall property or should remain in effect for a fixed or indefinite period of time.

2. The Motion for an Order Pursuant to 11 U.S.C. §543(d)(1) to Excuse Custodian From the Requirements of 11 U.S.C. §543(a) and 11 U.S.C. §543(b) filed by Wells Fargo, as Trustee for the registered holders of Morgan Stanley Capital I, Inc., Commercial Mortgage Pass-Through Certificates, Series 1999-FNV1, filed on January 22, 2004, is DENIED.

3. John Cheadle, the receiver appointed on November 24, 2003, by the Chancery Court for Sevier County, Tennessee, shall: (1) turnover all rents collected from his operation of the Governor's Crossing Outlet Mall to Wells Fargo Bank Minnesota, N.A. within ten (10) days; (2) file the accounting required by 11 U.S.C.A. § 543(b)(2) (West 1993) within fourteen (14) days; and (3) file any application seeking compensation and expenses as contemplated by 11 U.S.C.A. § 543(c)(2) (West 1993) within thirty (30) days.

4. Commencing in May, the Debtor shall provide Wells Fargo Bank Minnesota, N.A. with itemized monthly statements, due on the 10th day of June and on the 10th day following each reporting month thereafter, showing all income collected from any source, excluding tenant rents, and all operating expenses of every kind and description.

5. The Debtor shall continue collecting rents from all tenants of the Governor's Crossing Outlet Mall, but shall account for and remit all such rents to their owner, Wells Fargo Bank Minnesota, N.A., at such times and under such conditions as may be mutually agreed upon by the parties.

6. Wells Fargo Bank Minnesota, N.A. shall, by May 31, 2004, provide the Debtor with a report showing how it applied all funds distributed to it by the receiver toward satisfaction of the Debtor's obligation under the December 24, 1998 Promissory Note that forms the basis of its claim. Wells Fargo Bank Minnesota, N.A. shall thereafter file monthly reports, by the

10th day of each month, commencing on June 10, 2004, showing all rents received from the Debtor and the application of those rents toward the indebtedness, for the month preceding the report.

SO ORDERED.

ENTER: April 29, 2004

BY THE COURT

/s/ Richard Stair, Jr.

RICHARD STAIR, JR.
UNITED STATES BANKRUPTCY JUDGE